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THE SECRETARY OF HEALTH AND HUMAN SERVICES
WASHINGTON, D. C. 20201

MAY 10 1994

The Honorable Albert Gore, Jr.
President of the Senate
Washington, D.C. 20510

Dear Mr. President:

Section 1886(e)(3)(B) of the Social Security Act (the Act) requires that the Secretary of Health and Human Services report to Congress the initial estimate of the applicable percentage increase for FY 1995 that she will recommend for hospitals subject to the Medicare prospective payment system (PPS) and for hospitals and units excluded from PPS. This submission constitutes the required report.

Our recommendations are consistent with the provisions of the Omnibus Budget Reconciliation Act (OBRA) of 1993. For FY 1995, we recommend an average update for all hospitals subject to PPS equal to the percentage increase in the hospital market basket (an index of inflation in goods and services used by hospitals) minus 1.4 percentage points. We currently estimate that the market basket rate of increase for FY 1995 will be 3.6 percent. The average update for all PPS hospitals would equal 2.2 percent (the market basket percentage increase of 3.6 percent minus 1.4 percent).

We are recommending the updates for urban and rural hospitals that are provided under current law. Under our recommendation and OBRA 1993, urban PPS hospitals would receive the market basket rate of increase minus 2.5 percentage points, or a 1.1 percent increase. Rural PPS hospitals would receive the market basket rate of increase plus 4.8 percentage points, or 8.4 percent. We currently have separate PPS payment rates for large urban, other urban and rural hospitals. However, the law requires us to eliminate the separate rural rate and to establish a single rate for rural and other urban hospitals beginning in FY 1995. The higher update for rural PPS hospitals eliminates the difference between the rate paid to other urban and rural PPS hospitals.

Sole community hospitals (SCHs) are the sole source of care in their area and are afforded special payment protection to maintain access to services for Medicare beneficiaries. SCHs are paid the higher of a hospital-specific rate or the Federal rate. Under our recommendation and OBRA 1993, the update to hospital-specific rates will equal the market basket rate of increase minus 2.2 percentage points or 1.4 percent.

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Hospitals and units that are excluded from PPS are paid based on reasonable costs subject to a limit under the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982. Consistent with current law, we recommend an increase in the TEFRA limit equal to the rate of increase in the excluded hospital market basket (3.7 percent) minus 1.0 percentage points, or 2.7 percent.

Our recommendation for the updates is based on current projections of relevant data, and is consistent with the President's budget. A final recommendation on the appropriate percentage increases for FY 1995 will be made nearer the beginning of the new Federal Fiscal Year based on the most current market basket projection available at that time. The final recommendation will incorporate our analysis of the latest estimates of all relevant factors, including recommendations by the Prospective Payment Assessment Commission (ProPAC).

Section 1886(d)(4)(C)(iv) of the Act requires that the Secretary include in her report recommendations with respect to adjustments to the diagnosis-related group (DRG) weighting factors. At this time, we do not anticipate recommending any adjustment to the DRG weighting factors for FY 1995.

I am pleased to provide my recommendations to you.

Sincerely,



Donna E. Shalala



THE SECRETARY OF HEALTH AND HUMAN SERVICES
WASHINGTON, D. C. 20201

MAY 10 1994

The Honorable Thomas S. Foley
Speaker of the House of Representatives
Washington, D.C. 20515

Dear Mr. Speaker:

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Sincerely,



Donna E. Shalala

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